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VIA ECFS

Marlene H. Dortch, Esq.
Secretary
Federal Communications Commission
445 12th Street, S.W.
Washington, D.C. 20554

Re: Notice of Ex Parte, *Implementation of Section 621(a)(1) of the Cable Communications Policy Act of 1984 as Amended by the Cable Television Consumer Protection and Competition Act of 1992*, MB Docket No. 05-311

Dear Ms. Dortch,

NCTA – The Internet & Television Association submits this letter in further response to arguments and issues raised by commenters in this proceeding.[1]

Section 626 Renewal Criteria and Franchise Fee Cap

Some commenters have conflated the franchise renewal standards in Section 626(c)(1)(D) of the Cable Act with the separate statutory cap on franchise fees under Section 622,[2] arguing that the language in Section 626(c)(1)(D) requiring franchising authorities to take into account the costs of meeting cable-related community needs and interests would be superfluous if nonmonetary exactions were capped by the franchise fee. Contrary to the arguments of these commenters, Congress enacted *both* provisions as complementary measures to impose fiscal restraint on franchising authorities.

Section 626(c)(1)(D) imposes reasonableness and cost-benefit standards for assessing the "operator's [renewal] proposal." It requires franchising authorities to consider whether the proposal put forward by the cable operator "is reasonable to meet the future cable-related

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1 *Implementation of Section 621(a)(1) of the Cable Communications Policy Act of 1984 as Amended by the Cable Television Consumer Protection and Competition Act of 1992*, Second Further Notice of Proposed Rulemaking, 33 FCC Rcd. 8952 ¶ 1 (2018) ("*Notice*").

2 *See, e.g.,* Reply Comments of the Alliance for Communications Democracy et al. at 6-7 ("CAPA Reply Comments"); Reply Comments of Community Communications Consulting at 1; Reply Comments of the City of New York at 3; Reply Comments of the City of Newton, Massachusetts at 9-10; Comments of City of Philadelphia et al. at 30; Comments of Anne Arundel County et al. at 11.

community needs and interests, taking into account the cost."[3] Demands over and above the cable operator's proposal that a franchising authority makes as a condition of granting renewal must also be assessed against these standards, including whether the resulting costs outweigh the benefits.[4]

Complementing the general renewal standards in Section 626(c)(1)(D), Section 622 imposes a specific monetary cap on both initial franchise grants and renewal demands that fall within the broad definition of "franchise fee," including cable-related in-kind exactions (e.g., PEG operating support, public service announcements, free cable service, I-Nets, etc.). As the Commission has tentatively concluded, franchise fees are broadly defined under Section 622(g)(1) to include assessments "of any kind," including noncash exactions, excluding only PEG capital costs (i.e. costs for construction of PEG facilities) per Section 622(g)(2)(C).

Under Section 622, states or local communities have discretion to set priorities for franchise fee expenditures, and may elect to spend some of the franchise fees on in-kind exactions imposed in an initial franchise grant or through the franchise renewal process.[5] This is exactly the kind of balancing that Congress intended under the Act to protect cable operators and their subscribers from excessive taxation.[6]

To be sure, while Section 622(b) authorizes franchise fees "up to" five percent of cable service revenues, some franchising authorities have determined that they can satisfy reasonable community needs and interests in video programming at a *lower* cost and without levying the maximum five percent fee on cable subscribers. Unfortunately, most franchising authorities have improperly viewed the five percent franchise fee cap as a *floor* for monetary payments before adding on costly in-kind exactions – rather than as the *ceiling* that Congress intended.[7]

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3 *See* NCTA Reply Comments at 10 (discussing 47 U.S.C. § 546(c)(1)(D)).

4 *See* H.R. Rep. No. 98-934 at *74 (1984) ("in assessing the costs under this criteria, the cable operator's ability to earn a fair rate of return on its investment *and the impact of such costs on subscriber rates* are important considerations") (emphasis added).

5 *See* NCTA Comments at 41 (observing that the Cable Act definition of franchise fee "includes any tax, fee, or assessment *of any kind*," subject only to specific exceptions, and that "while franchising authorities and local governments may spend their five percent franchise fee in myriad ways, they may not (with the exception of small incidentals and [PEG capital costs]) exceed the five percent fee by demanding in-kind assessments").

6 *See* S. Rep. No. 98-67, at 25 (1983) ("The committee feels it is necessary to impose such a franchise fee *ceiling* because the committee is concerned that, without a check on such fees, local governments may be tempted to solve their fiscal problems by what would amount to a discriminatory tax not levied on cable's competitors.") (emphasis added).

7 *See* NCTA Reply Comments at 10-11; *id.*, Attachment 2, at 3-14.

Free or Discounted Services Required by Franchising Authorities

Some commenters have argued that free or discounted services demanded by franchising authorities should be valued at the "actual cost" to cable operators.[8] These arguments are flawed on both economic and legal grounds.

As the prior submission from NCTA's economists explains, in today's competitive marketplace, actual costs are simply not the proper method for determining the value of free or discounted services to franchising authorities or their designees from an economic perspective. Rather, any valuation method for such services must take into account *opportunity costs.*[9] While cable operators are required to provide courtesy services to franchising authorities and their designees for "free," the provision of those services is not "free" to the cable operator. The operator must dedicate network bandwidth, employee time, and other limited resources to providing "free" services to a franchising authority rather than allocating those resources toward other purposes.[10] The best available proxy for opportunity cost is fair market value.[11]

In contrast, an "actual cost" model would not capture the full transfer of value from the operator to the franchising authority, or the lost opportunity to the cable operator. Rather than paying fair market value for a particular service, the franchising authority would just be paying incremental cost, while the cable operator would sustain a greater loss.[12] In other words, the cable operator would be transferring uncompensated value to the franchising authority (the delta between fair market value and actual cost). This would result in a lower return on investment and reduced incentives to offer new services and other consumer benefits (e.g., broadband speed increases, free Wi-Fi, other promotions and discounts).[13]

For the same reasons, a cost-based approach would be inconsistent with the statutory five-percent cap on franchise fees from a legal perspective. For example, like monetary payments, free or discounted services are a form of compensation to franchising authorities for use of the public rights-of-way ("ROW") to operate a cable system and must be included in the five-percent cap. With the growth of video competition, franchising authorities have alternatives in the marketplace for these services and would have to pay fair market value for them from any other provider. Thus, the value of these services from a cable operator, as part of the compensation it pays to franchising authorities for use of the public ROW, should reflect their fair market value and must be accounted for within the five-percent cap.[14] Reaffirming proper

8 *See, e.g.,* Comments of Cable Act Preservation Alliance ("CAPA") at 14; CAPA Reply Comments at 2, 16-17; Comments of City of Philadelphia et al. at 4, 38.

9 *See* NCTA Reply Comments, Orszag/Shampine Economic Analysis ¶ 20.

10 *See id.* ¶¶ 20-22 (explaining tradeoffs inherent in dedicating cable system bandwidth and other resources to in-kind demands).

11 *See id.* ¶ 21.

12 *See id.* ¶ 20 ("In general, in-kind demands have an impact on investment incentives greater than their direct out-of-pocket cost.").

13 *See id.* ¶¶ 40-48 (discussing how decreasing returns on investments will decrease incentives to invest in broadband deployment and other network improvements).

14 *See* NCTA Comments at 52.

application of the statutory cap on franchise fees is essential in today's highly competitive marketplace, where other intermodal competitors and their customers typically do not bear the costs of such franchising obligations.

This market-based approach is also consistent with Congress's express mandate to eliminate rate regulation whenever effective competition exists, which today is virtually nationwide.[15] The cost-based approach for courtesy services advocated by some franchising authorities would be a form of price regulation that takes a giant step backwards rather than forwards under the statutory scheme.[16] It would force cable operators and their subscribers to continue to subsidize these services and perpetuate the intermodal competitive imbalance in the marketplace that this proceeding is intended to redress.[17]

Further, some franchising authorities have advocated for a cost-based approach by citing to the Commission's recent small cell order. That comparison is inapt, but it helps prove the relevant point here. Because local governments hold a monopoly over ROW access, there is no "market value" for this "service." Thus, in the small cell order, the Commission properly looked to the costs of providing access to the ROW.[18] As the Commission recognizes, however, cable monopolies are long gone. Intermodal competition establishes market rates for these services now, and Congress expressly intended for the marketplace – not price regulation – to set those values in such circumstances.

Finally, there are tens of thousands of cable franchises across the country.[19] As NCTA has shown in this proceeding, in-kind contributions vary from franchise to franchise, and may include significant numbers of courtesy accounts, extensive I-Nets, substantial PEG operating support, public service announcements, free advertising time, and others. The extensive examples of in-kind contributions already submitted into the record by NCTA are representative of the pervasiveness and variation of such exactions. While our member companies do not track these different categories of in-kind contributions in a manner that permits percentage calculations, one cable company broadly estimates that 80-90% of franchises impose some level of free video services, 30-40% require multiple return lines, and 5-10% include I-Net obligations

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15 *See Amendment to the Commission's Rules Concerning Effective Competition; Implementation of Section 111 of the STELA Reauthorization Act*, Report and Order, 30 FCC Rcd 6574 ¶ 1 (2015).

16 *See* NCTA Reply Comments at 20-21.

17 Implementing an "actual cost" regime would also be an administrative morass, requiring cable operators to provide detailed cost and rate-of-return calculations to justify pricing decisions in ways that were never contemplated under the Cable Act, despite the ready availability of pricing for analogous retail services. In fact, cable operators already offer retail services that provide readily-available, transparent, market-based valuations for in-kind exactions (e.g., rate card pricing for cable services). *See* NCTA Comments at 53-55.

18 *Accelerating Wireless Broadband Deployment by Removing Barriers to Infrastructure Investment et al.*, Declaratory Ruling and Third Report and Order, 33 FCC Rcd. 9088 ¶¶ 55, 73 (2018); *see also Accelerating Wireless Broadband Deployment by Removing Barriers to Infrastructure Investment et al.*, Order Denying Motion for Stay, WT Docket No. 17-79 et al., DA 18-1240 ¶14 n.47 (WTB Dec. 10, 2018) ("[T]here is no 'market value' of assets that are not freely bought and sold in a free 'market'; and in such cases, use of actual costs or other readily-discernable amounts are not unreasonable proxies for estimating a market value that would be 'fair' if a market existed.").

19 *See also* Remarks of William E. Kennard, Chairman, FCC, Before the National Cable Television Association, *The Road Not Taken: Building a Broadband Future for America* (June 15, 1999) (estimating, before the advent of state-level video franchising, that "[t]here are 30,000 local franchising authorities in the United States").

(which, while a lower percentage, are large in-kind contributions that also involve significant additional operating costs for cable companies and subscribers).

This letter is being filed electronically pursuant to section 1.1206 of the Commission's rules. Please direct any questions to the undersigned.

Respectfully submitted,

/s/ Rick Chessen

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